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IN THE

SUPREME COURT OF THE UNITED STATES

155

OCTOBER TERM, A. D. 1963

No. [redacted]

MAURICE J. BREEN and ALYCE J. BREEN,
Petitioners,

vs.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE EIGHTH CIRCUIT

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To the Honorable Chief Justice and Associate Justices of the Supreme Court of the United States:

Your Petitioners pray that a Writ of Certiorari issue to review the judgment and decree of the United States Court of Appeals for the Eighth Circuit entered in the above entitled case on February 26, 1964.

OPINION

The opinion of the Tax Court is reported as T.C. Memo 1962-230. The opinion of the Court of Appeals is reported at 328 F.2d 58.

JURISDICTION

Judgment and Opinion of the Court of Appeals was entered on February 26, 1964. The jurisdiction of this Court is invoked under the provisions of 28 U.S.C.A., Sec. 1254 (1).

EXTENSION OF TIME TO PETITION

On the 30th day of April, A.D., 1964, the Honorable Byron R. White, Associate Justice of the Supreme Court of the United States, made an order extending the time for filing of the Petition for Writ of Certiorari in the above case to June 25, 1964.

QUESTIONS PRESENTED

Question I. Whether the taxpayer was entitled, with respect to a $4,200.00 fee received in 1955, to the benefit of the spreading provisions of Section 1301 of the Internal Revenue Code of 1954, 26 U.S.C.A. 1301.

Points

(a) Was the meaning of Sec. 107 (a) of the 1939 Code (spreading of personal services income) altered by Section 1301 in the 1954 Code?

(b) What significance, if any, can be attached to the words "to effect a particular result" (Sec. 1301 (b)

of 1954 Code) with reference to the personal services of corporation officers?

(c) If Sec. 1301 of the 1954 Code modifies or limits the spreading of income by corporation officers for personal services, should it be applied retroactively to income earned prior to 1954 while Sec. 107 (a) of the 1939 Code prescribed the rights of such officers?

Question II. Whether gains the taxpayer realized in 1955 and 1956 on two trustee's certificates were ordinary income, or were long-term capital gain, under the provisions of Section 318, Par. a (2) (B) Section 302 and Section 331 of the Internal Revenue Code of 1954.

Points

(a) Corporate liquidating dividends are paid to a Trustee who is holding the corporation stock for six beneficiaries, each of whom has a Trustee's Certificate showing his specific fractional interest in all of the stock so held by the Trustee.

(b) The Trustee transfers .5054 percent of the total of the liquidating dividends to one beneficiary, who held two certificates that totaled .5054 percent interest in all the stock held by said Trustee.

(c) The six months limitation and the capital asset feature are conceded.

(d) Does this certificate holder realize long-term capital gain on the profit between the "cost to him" and the "total of the liquidation dividends" paid by the trustee to him, or is he a "claimant" as against the Trustee and therefore the corporate liquidating dividend passed on to him for his proportionable share of his corporation stock, is nothing more than a payment on his *claim against the Trustee* and therefore *ordinary* income?

(e) Or again—the question may be stated, were these certificates delivered by the Trustee in 1931, negotiable pledges representing a certain fractional ownership in corporate stock held by the Trustee for the certificate holders, or were they nothing more than "claims" against the Trustee?

STATUTES AND REGULATIONS INVOLVED

Division I

Code Section 1301 (b).

"An employment means an arrangement, or series of arrangement, for the performance of personal services by an individual or partnership, to effect a particular result, regardless of the number of sources from which compensation therefor is obtained".
28 U.S.C.A., 1301.
Section 107 (a) of the 1939 Code, as amended.

Division II

Section 302 of the 1954 Code, provides:

"Sec. 302. Distribution in Redemption of Stock. (a) General Rule.—If a corporation redeems its stock (within the meaning of section 317 (b)), and if paragraph (1), (2), (3), or (4) of subsection (b) applies, such redemption shall be treated as a distribution in part or full payment in exchange for the stock".

Subsection (3) provides:

"(3) Termination of shareholder's interest.—Subsection (a) shall apply if the redemption is in complete redemption of all of the stock of the corporation owned by the shareholder".
Identified as 26 U.S.C.A., Section 302.

Section 331 of the 1954 Code provides:

"GAIN OR LOSS TO SHAREHOLDERS IN CORPORATE LIQUIDATIONS.

(a) General Rule.—

(1) Complete liquidations.—Amounts distributed in complete liquidation of a corporation shall be treated as in full payment in exchange for the stock".
26 U.S.C.A., Section 331.
Code Section 652 (b).

Section 662 (b) of the 1954 Code:

"The amounts determined under subsection (a) shall have the same character in the hands of the beneficiary as in the hands of the estate or trust".

POINTS AND LAW SUPPORTING SAME

Division I

POINT 1.

Directing a corporation by a lawyer for the specific purpose of selling the one corporate asset so as to liquidate the company as soon and as advantageously as possible is "an employment" to effect a particular result.

1939 Code, Section 107 (a).
1954 Code, Section 1301; 28 U.S.C.A. 1301.
Wattley v. *C.I.R.*, 275 F.2d 461.

POINT 2.

Congress intended no change in Section 107 (a) of the 1939 Code in enacting Section 1301 of the 1954 Code; 28 U.S.C.A. 1301.

Wattley v. *C.I.R.*, 275 F.2d 461.

POINT 3.

Statutes affecting change in substantive rights will not be given a retroactive effect.

New York Life Ins. Co. v. *Truesdale,* (4th Cir.) 79 F.2d 481.

82 C.J.S., page 994.

POINT 4.

In the absence of definite indication of a legislative purpose to that end, the re-enactment of a statute does not affect its meaning or enlarge its scope, nor does mere change in language necessarily indicate an intention to change the law.

82 C.J.S. 845.

Wattley v. *C.I.R.*, 275 F.2d 461.

Division II

POINT 1.

A "sale" in respect to being the third requirement for a long-term capital gain treatment is often supplied by a "statutory sale"—a condition that is a substitute for a conventional sale—by the Internal Revenue Code.

1954 Section 302; 26 U.S.C.A. 302.

1954 Section 318; 26 U.S.C.A. 318.

1954 Section 331 (a); 26 U.S.C.A. 331.

POINT 2.

Liquidating dividends retiring capital stock create a "sale of exchange".

1954 Code, Section 302; 26 U.S.C.A. 302.

POINT 3.

What is capital gain to a trustee is passed on as capital gain to the beneficiary.

1954 Code, Section 652(b); 26 U.S.C.A. 652.

Code, Section 662 (b); 26 U.S.C.A. 662.

Rev. Rul. 56-78, IRB 1956, 10, 27; also referred to as Rev. Rul. 56-78, C.B. 1956-1, 648.

CONCORDANCE OF 1954 CODE AND 1939 CODE WERE ESSENTIAL

1954 Code, Section 1301.

1939 Code, Section 107 (a), as amended.

1954 Code, Sections 651, 652, 661, 662.

1939 Code, Section 162 (b).

STATEMENT OF FACTS

Foreword

Petitioner has no illusions in respect to a Petition for a Writ of Certiorari in this Court, but again I think that I understand the frame of mind of the midlands taxpayers, most of whom have no facilities to question, or engage in any protracted litigation with the Internal Revenue Service, because it necessarily means long, costly and generally unsatisfactory litigation, because at all times at the lower levels the taxpayer is trying his case to his "adversary", so that by the time he (the taxpayer) reaches a conventional tribunal, that is not directly or indirectly related to the Internal Revenue Service, he is pretty well whipped, spirit-wise and money-wise—in fact, substantially all "resisters" are long gone before they reach a conventional court.

After the taxpayer has had his hearing before the Regional Commissioner and "observer"—not necessarily in his home state—he eventually receives Exhibit "C", and along with that is some advice—that we assume is supposed to be cheerful and sort of buoying (Par. 2, L-1 of last page of Ex. "C"). "The Tax Court of the United States is in no way connected with the Internal Revenue Service or Treasury Department". Either "true or false" (as the school examinations now say) it carries implications that are not too good.

Again—if the taxpayer is stubborn and persistent and struggles through a series of defeats, he is often confronted with an atmosphere, in the conventional courts, that indicates that the Court prefers to defer to the "experts" in the Tax Service (*Samuel Towers*, 24 T.C. 199, 247 F.2d 233; *Commissioner* v. *Bedford*, 325 U.S. 283).

We presume this same reasoning could be applied to the various other "bureau" tribunals, and it will be a sad day in America, if the time ever comes that the Courts make it a "rule" to "defer" to the "head tribunal" of these various agencies.

Division 1 (Spreading of Fees)

Involves the right of the petitioner. Maurice J. Breen, a lawyer, to spread a fee, or compensation, of $4,200.00 received in 1955, over the period of years during which it was earned, under the provisions of Section 1301 (b) of the Internal Revenue Code of 1954.

Generally speaking the Circuit Court raised no question about compliance with either the "thirty-six months requirement" or the "80% requirement" (Op. Page 8, Par. 2), but held against the taxpayer, on the theory that the services were not "an employment" (Op. page 19,

Par. 1), within Section 1301 (b) of the 1954 Code, which is said by the Court to have modified the statute that had been controlling (1939 Code, Sec. 107 (a)), prior to 1954. The services were performed after 1930 (Exhibit 8).

Whether the services were "an employment" under the provisions of Section 1301 (b) of the 1954 Code is an issue, and Exhibit 8 also shows that the services for which the $4,200.00 was paid were performed and earned before 1954, while and when Sec. 107 (a) of the 1939 Code prevailed, without the debatable modification of the 1954 Act.

The work, or services referred to, involved the holding title to *facilitate the holding and selling* of a 220 acre tract of coal land (which produced royalty) adjacent to the City of Des Moines, Iowa, and which had been owned by one Denis M. Kelleher of Fort Dodge, Iowa, and your petitioner, in a fiduciary capacity. Your petitioner was at all times president of the new holding corporation, and Kelleher was vice-president, and his wife, Mary S. Kelleher, secretary and treasurer. The *idea* ultimately served its purpose, as the coal royalties paid to the holding corporation provided the necessary funds to pay interest, taxes and mortgage payments, to avoid foreclosure, *until the time came*, when the land could be, and was sold for subdivision purposes for a Des Moines suburb (Exhibit 5 and Exhibit 6) (Transcript Page 9, Line 8 to Page 12, Line 20; Page 31, Line 20 to Page 33, Line 4).

The taxpayer was not interested financially in the company and, as far as duties involved the corporation, he was a "figure head" (the corporation) had no employees—and the so-called "officers" drew no salaries. Taxpayer's mission was to sell the land and liquidate the corporation and the stock.

This task took time—on account of the depression—but it was finally accomplished—but the Court held that it

was not an "employment" to "effect a particular result" because the taxpayer was listed as an officer and director of the corporation, that obviously could have no duties for its so-called "officers" to perform.

As a matter of fact, the taxpayer—as a lawyer—handled this Urbandale situation in the same fashion as he did, or would, any long drawn out legal matter. As a lawyer—and that is all—he had this Urbandale situation thrust upon him and there was no other solution available to him, except to sell the land and liquidate the holding company.

Division 2 (Capital Gain on Stock Certificates)

The second problem (*and more important issue*) concerns the right of Maurice J. Breen to report a profit of $18,943.29 that he made on the purchase of two Trustee's Certificates in 1955-1956, as "long-term capital gain" and not as "ordinary income".

It was conceded by the Circuit Court:

> "that the certificates were capital assets under Sec. 122's general definition of 'property held by the taxpayer'. And they were held by this taxpayer more than six months. The inquiry then is only whether the gain resulted from a 'sale or exchange'." On Pages 11-12.

These certificates were purchased by the petitioner in the spring of 1954 (Ex. 13 and Ex. 15), and each certificate represented a specific, fractional, "equitable ownership and beneficial interest" in 500 shares of Urbandale Company capital stock held by the Bank, as Trustee, for the benefit of six Certificate holders. One of these Certificates so purchased represented a .4666 interest, and the second Certificate a .0384 interest (Ex. 10 and Ex. 14), so that after

the purchase, the taxpayer owned a trifle more than a 50% interest in the 500 shares of the Urbandale Company stock held by the Bank-Trustee.

In 1955, the Urbandale Coal Company sold its one asset, that is, its interest in the 220 acre tract adjacent to Des Moines, for subdivision purposes, and it then *immediately liquidated* the Urbandale corporation, and retired all the capital stock by paying out all of the net receipts from the land sale as a liquidating dividend—one-half to the Bank-Trustee and one-half to Kelleher. The complete liquidating dividends received by the Bank-Trustee were in turn immediately *passed on* to the six Certificate holders (Ex. "B" of Ex. 6), and the liquidation of the corporation which began March 22, 1955, was closed December 31, 1955 (Trans. p. 16, ll. 1 to 8) and the final payment of the liquidating dividends by the Bank-Trustee (January 15, 1956) in turn resulted in the liquidation of the trusteeship (Ex. 16).

The Petitioner in April of 1954 purchased these two certificates for the sum of $2,650.00; when the corporation was liquidated, he received $8,258.00 in 1955 and $13,334.41 in January of 1956, as liquidating dividends on said corporation stock. That liquidated both the corporation and the trust (Final Report of Trustee, Ex. 6).

The two Trust Certificates (Exhibit 10 and Exhibit 14) above referred to were identical, and recited at the beginning of each certificate:

> (Ex. 10) "This certifies that First National Bank of Fort Dodge, Iowa, is the owner of a .4666 of the equitable ownership and beneficial interest in * * * two hundred and fifty (250) shares of the preferred stock and two hundred and fifty (250) shares of the common stock of the Urbandale Coal & Acreage Company of Fort Dodge, Iowa, title to which certificates

of stock is held by the First State Bank & Trust Company of Fort Dodge, Iowa, as trustee for the benefit of the holder or holders of this certificate and all similar certificates issued or to be issued by the trustee to evidence ownership of said beneficial interest in said property so held by it in trust" (Ex. 10).

During the years that the land was being held awaiting sale (1931 to 1947), many coal royalty dividends were paid, and treated as ordinary income (See Preamble to Exhibit "A" attached to Exhibit 6). In 1955 *the one asset* that the Urbandale corporation owned, to wit, the 220 acres of land, was sold, and the corporation completely liquidated, and the corporate stock *retired,* in about nine months time. One-half of the liquidating dividends were paid to the trustee and immediately passed on to the certificate holders in accord with their respective interests (Ex. "B" of Ex. 6, last 15 debits).

We quote the first six lines from "Exhibit A" attached to Exhibit 6 (the Trustee's Final Report), to wit:

> "Receipts by the trustee from the dividends from the operation, and *also the sale and liquidating dividends* of Urbandale Coal & Acreage Company. All of the receipts listed below, which were received by the Trustee, were immediately distributed in full". (Our emphasis).

All of the payments received by petitioner in liquidation of his two Certificates, which he purchased in 1954, were *liquidating* dividends paid by the corporation to the Trustee in liquidation and retirement of the stock held in trust *for the Certificate holders* and was immediately passed on by the Trustee to the Certificate holders, or beneficiaries, as liquidating dividends (Ex. 6, see Ex. "A", attached to Ex. 6).

Notwithstanding the fact that all of the money received by this petitioner after he purchased the two Certificates in 1954 was paid in liquidating dividends in 1955-1956, the Circuit Court held that this money was *ordinary income*.

Naturally, the Circuit Court has to come up with some explanation that would support his notion that liquidating dividends on corporation stock could be said to be "ordinary income".

There was no escape from the fact that these 1955-1956 payments from Urbandale to the trustee, and from the trustee to the six certificate holders, amounting to approximately $40,000, were in fact *liquidating dividends*, so naturally any "adjustment" had to be made with reference to the nature of the certificates and, of course, any "nature" that would be compatible with the Court's ruling would have to be something other than a fractional interest in the corporate stock that was being liquidated.

We assume the Circuit Court was not very happy with the reasoning of the Tax Court, because the Tax Court Judge worked his woy out of the *same situation* by calling the certificates "trustee's notes". Apparently the Circuit Court did not want to go along with that idea.

The new theory by the Circuit Court in substitution of the "Trustee's notes" notion, was to christen Exhibits 10 and 14 "Claims against the Trustee". It isn't too clear-cut, the general idea was that the six original claimants against the estate really didn't release their claims against the estate—even though Exhibit 5 and the Probate Record so provided. The "plan" was that these were sort of "partial releases"—applying to some of the estate property —but not to the part that they bought in at an open sale from the executor and estate.

Again, the sale, the deeds, et cetera, in consideration for the releases were in fact not ready sales or deeds, and this, of course, ultimately becomes pretty involved as a theory—but at any rate it was sufficient to support the Commissioner—just as the Tax Court's fiction about the "Trustee's notes" served the same purpose.

So the new plan is rather involved, but in substance it begins with the releases by the creditors in the Merritt estate and, although the releases were *absolute* as evidenced by Exhibit 5, page 9, Par. 1, which directs the trustee in payment of ($27,500 in claims) the purchase of the Merritt land, and some worthless bank stock from the estate, by the six large creditors to:

> "pay the purchase price therefor in the manner therein designed and expressed, viz. by surrendering, discharging and releasing the several claims of the First National Bank, Doris O. Merritt, Margaret Merritt, Olive Seay, Edna Richardson, Catherine Carey and Bridget Carey, and by executing the requisite contracts, vouchers and other instruments to evidence such discharge, satisfaction and release of said claims, in consideration of the application of the amount thereof upon the purchase price by said trustee bid for said property."

Notwithstanding the facts set forth above, and also in other parts of Exhibit 5, the absolute release of the claims on the court record, and the *deed by the executor* to the trustee of the land, and the immediate subsequent *deed by the trustee to the Urbandale company* (Trans. p. 10, l. 10 to l. 12), the Court said speaking of these releases by the six creditors, the sale and the deeds:

> "this, however, we do not construe and interpret as effecting a novation or basic change in the posture of the six creditors and their successors." (Op. p. 14, l. 33).

Again, the trust certificates recited in the very beginning, and in no uncertain terms (Exhibits 10 and 14) what they were. For instance, Exhibit 10 (and they were all alike except as to the name of the beneficiary, and the fractional interest in the trust):

> "This certifies that the First National Bank of Fort Dodge, Iowa, is the owner of a .4666 of the equitable ownership and beneficial interest in" (Exhibit 10),

and then goes on to describe the several stocks, only one of which is of importance because the others were worthless bank stock. However, the Circuit Court disposed of this hurdle (Op. p. 12, last paragraph):

> "It is true that each certificate recites that the holder 'is the owner of (a stated percentage) of the equitable ownership and beneficial interest in', named stocks, including Urbandale, 'title to which' is held by the trustee 'for the benefit of the holder'. *But labels do not determine ultimate character.*" (Our emphasis).

The Circuit Court did not attempt to explain the record (Trans. p. 10, l. 10); that the Merritt estate had deeded the land in question to the trustee, the trustee in turn had deeded it to the Urbandale company, and the Urbandale company had with the approval of the State Executive Council issued 1000 shares of stock against the land, of which one-half went to the trustee and one-half went to Kelleher.

Notwithstanding the directness and plainness of the record over the release of the claims, the sale of the land, and the forthright language of the certificates themselves, the Court still had another problem in that in 1952 the beneficiaries of the W. N. Merritt estate, *all of whom were still alive and legally competent* (Ex. 21, p. 1, l. 7), gave a quit claim deed to the Urbandale company releasing any

claim, or purported claim, that they might have, as against the land or the stock. (This is Exhibit 21; also Trans. p. 31, ll. 1 to 9). Again, this deed had to be explained, because, of course, from 1952 on *nobody* had a claim of any kind to this land, or the stock issued against it; that is, after that deed was executed, the rather *fantastic lien* that the estate beneficiaries originally had, as to this Urbandale land was eliminated, and that was some two years before this taxpayer bought these certificates.

But the Circuit Court again disposed of this obstacle, at least to his own satisfaction, by saying (Op. p. 15, second paragraph):

> "Neither do we regard as opposingly significant the quit claim deed executed by the will beneficiaries in 1952 before the taxpayer's acquisition of the two certificates in 1954 * * *. Had the deed been intended to operate as a release of the will beneficiaries interest under the agreement, it is reasonable to assume that broader provisions to that effect would have been forthcoming."

This statement is made notwithstanding the *Transcript Record* when counsel for the Commissioner asked (Trans. p. 31, l. 1):

> "Q. Now, then, they also in consideration of that release their rights to the trust agreement. Is that correct?
> A. That's right."

The Court, after disposing of these four rather outstanding obstacles in more or less of an arbitrary fashion, took the final stand that these Trust Certificates, Exhibits 10 and 14, were not what they said they were, but they were sort of "partial claims" (Op. p. 15, l. 4, first paragraph):

> "Instead of being applicable to all the assets of the decedent's estate, they became confined to those

> fewer assets which had come from the estate to the trustee by way of the 'purchase', and pursuant to the understanding reached by all concerned. The release of the claims therefor had significance only as it freed untransferred assets of the estate from the claims of the six major creditors. These creditors' claims were still directed to the transferred assets."

Notwithstanding that the written record is directly opposed to the Court's theory, it is also a little bit strained as far as the principles of ordinary logic and human behavior are concerned in that this whole situation was set up with a background of an insolvent estate and six creditors that couldn't be paid. They *then* had a lien on the *whole estate*, and it is rather difficult to get the Court's "plan", based on the notion that these six creditors, of what there appeared to be an insolvent estate, became "big hearted" and gave up part of what they *already* had.

That isn't human nature, and moreover it isn't the record in this case, but possibly it is a better theory than the "trustee's notes" put forth in Exhibit C, and also by the Tax Court Opinion pages 19 and 20.

REASONS FOR GRANTING WRIT AND ARGUMENT IN SUPPORT

I

(Interpretation of 1954 Code, Sec. 1301)

The First Division involves the spreading of fees for personal services, and particularly the interpretation of Section 1301 (b) of the 1954 Code, particularly with reference to the "employment" of corporate officers.

We would assume that this was a matter of considerable importance as gauged by the frequency with which

spreading of "bunched income" occurs, and this Opinion for all practical purposes (in fact any purposes) eliminates any one designated as a corporate officer from the benefits of the Act.

Countless cases at all three levels of the Federal Courts approved the spreading of compensation received by corporate officers under the provisions of Section 220 (a) of the Revenue Act of 1939, and again as amended by Section 139 (a) of the 1942 Act, but under this Opinion the Court holds that Section 107 (a) of the 1939 Code was materially changed by the 1954 Act, and that a corporate officer was a "*general* employment" and not qualified as such, to to come within the definition "to effect a particular result".

At the time this Opinion was written, the case of *Wattley* v. *The Commissioner*, 275 F.2d 461 (2 Cir. 1960), had held that Congress in enacting Section 1301 of the 1954 Code had no intention of changing, or altering the prevailing principles under Section 107 (a) of the 1939 Code.

It would appear highly important to determine whether or not the 1954 Act (Sec. 1301) by the words "to effect a particular result" completely changes the statute, or possibly those words were intended merely *at most* to eliminate the questionable practice of attempting to "string together" several, separate and distinct employments.

In this instance the whole record shows beyond dispute that this small corporation *itself* was set up to be liquidated as soon as possible, and the taxpayer was the sole liquidating agent, with no interest of any kind in the corporation except that he served as a *nominal* officer and director. By the terms of the Circuit Court Opinion the taxpayer's "official position" made him *ineligible* to spread his compensation as a "director and liquidating agent" Exhibit 8. Par. 3.

We quote from page 10, Paragraph 3 of the Circuit Court Opinion:

> "*Wattley* (*Wattley* v. *Commissioner, supra,* 275 F.2d 461 (2 Cir. 1960)) would support the taxpayer's position here were his employment made, as he contends, only to effect the sale of the Polk County real estate. But his activities were broader than that. He was a director and an officer and the management force behind Urbandale."

In short, the *Wattley* case, from the Second Circuit in 1960, says there is no change in the spreading of fees for personal services, while this Opinion in the Eighth Circuit eliminates all corporate officers from spreading a compensation even though the employment might be to "effect a particular result" relating both to the corporation and the taxpayer personally. If he is a corporate officer, his work is *general.* Therefore he cannot qualify.

The corporation formed was not an ordinary conventional corporation, and the duty of your petitioner was not that which would be performed by a managing officer of a conventional, commercial corporation, because as shown by Exhibits 5 and 6, and the Transcript page 9, line 8 to page 12, line 12, this corporation was created in an emergency brought on by the depression (Ex. 6, p. 2, l. 5, p. 4, l. 18) in the late twenties and early thirties, half of its stockholders, in fact exactly half, were forced into the corporation to try to salvage this land near Des Moines, and the largest one of these "unwilling" stockholders was the First National Bank of Fort Dodge, Iowa, which had closed about the time of the organization of the corporation (Ex. 6, p. 4, third line of second paragraph), so it would seem perfectly obvious that this Urbandale corporation had but one purpose, one particular result to effect, and that was to sell this land as advantageously as possible.

and your petitioner, as a lawyer, was attempting to work out this *particular result*, but it took considerably more time and effort than he had originally expected.

There are *many* cases under the 1939 Code Section 107 (a) dealing with "bunched" income of an officer, manager or director of a corporation, being spread over the years in which it was earned.

Now, then, apparently this Court has in mind (under Sec. 1301 (b)) that the management of *any* corporation is not "an employment" to effect a particular result, and he even applies this to a situation where the *corporation itself* has but one objective.

There are two cases that we find, decided since the Code of 1954 became effective relating to this particular question, Sec. 1301 (b).

One is *Ranz* v. *C. I. R.*, 6th Circuit, 273 F.2d 810. A taxpayer was a sales agent for machine tools—no particular object in mind—just selling *any* tools to *any purchasers* he could find. The court held it was not an employment, because it was not designed to effect any *particular result*—just the routine business of selling tools.

Then there is still a later case of *Wattley* v. *C. I. R.*, 275 F.2d 461 (1960). It is rather an unusual case and somewhat similar to the case at bar, because the taxpayer was attempting to spread a commission for making a long-term lease that involved the Mutual Life Insurance Company and Manufacturers Trust Company. Apparently the taxpayer worked some nineteen years on the deal, and he finally made it. The Tax Court held against him on the theory that he had not qualified under the 80% rule as he had received a substantial amount of money from the corporation, by whom he was employed in the beginning while working on this same deal. The Circuit Court of

Appeals (Second Circuit) reversed the Tax Court, and permitted him to spread the fee over the years from 1944 to 1951, because during those years he collected no compensation from the corporation, and apparently the Court regarded the work of completing the lease as being something that was designed to effect a particular result; in fact, the Court rather indicates that there isn't any change in particular between 107 (a) of 1939 Code and 1301 (b) of 1954 Code. We quote as follows:

> "If we were taking a fresh view of Sec. 107 (a), we would have difficulty in seeing what difference it makes whether the taxpayer was acting solely as a broker repre ative of the corporation or as an individual broker. Assuming that he was acting solely for the corporation, it is still true that the nature of his services necessarily contemplated alternative times of feast and famine. If the taxpayer had to nurse along the transaction involving the Fifth Avenue property for nineteen years until a lease was eventually consummated, on which a commission was paid, it is hard to see why other entirely separate transactions should be used by the Tax Court to defeat the application of Sec. 107 (a). It is a fact, which the government does not discuss in its brief, that though the present case is covered by Sec. 107 (a), this alleviating provision was revised somewhat in phraseology in Sec. 1301 of the Internal Revenue Code of 1954, 26 U.S.C.A., Sec. 1301. *But it appears that the Congress did not suppose that it was changing the meaning of Sec. 107 (a) when it was enacting Sec. 1301 in its present form.* See H.R.Rep.No. 1337, 83d Cong., 2d Sess. A289 (1954); S.Rep.No. 1622, 83d Cong., 2d Sess. 445-46 (1954). See also 1 P-H 1959 Income Tax par. 7960, Frank Stephen Ranz, 1958, 31 T.C. 91, affirmed by the Court of Appeals, 6 Cir., 1960, 273 F.2d 810." (Our emphasis).

As we have pointed out, this whole record clearly shows that whatever phrases and formalities might be

used, that there was only *one problem* that this petitioner had in mind, and that was to sell this 220 acres so that the Certificate holders could realize as much money as possible on their Certificates. The corporation itself was sort of an idle form—it had no employees, not even any paid officers. It, as a corporation, did nothing except to pay the interest, taxes and mortgage payments, and divide the net royalty from the coal between the trustee and Kelleher. Your petitioner's efforts at all times were devoted to selling the land and liquidating the corporation. He, under the circumstances, did this through the corporation name, as its agent and manager, and lawyer.

In the earlier days of the corporation a sale was pretty much impossible *on account of economic conditions*, and later on it became an *absolute necessity* as coal mining in Iowa had become unprofitable (Ex. 6, pp. 7 and 8).

A sale was finally accomplished, and your petitioner, who had never received any compensation for his efforts in helping this corporation, for the specific purpose of selling the land, was paid the sum of $4,200.00, and certainly he never had but one object from the time this corporation was formed, that is, one particular result, and that was to sell the land and liquidate the corporation, because it had served its purpose when the land was sold.

We believe this record shows without any question that all the petitioner's activities on behalf of the Urbandale company, whether referred to as president, director or liquidating agent, *related to his services as a lawyer working for a corporation, in which he had no personal interest, to sell the one asset the corporation had, and to liquidate it.* It was purely a solo operation just as much, or even more so than, one law suit dragging on over a period of years.

This petitioner had but one object, and that was to liquidate the Urbandale company, which could only be done by selling the land; that was his one mission that had to be accomplished in order to close the Urbandale case.

Again, assume that there is some distinction between these two sections, which apparently was not intended by Congress, we suggest that this work by the petitioner was done between 1930 and 1955 (Exhibit 8). Section 1301 was enacted in 1954. At the time the petitioner performed almost all of the services, they certainly were *personal services* under the multiple interpretation of Section 107 (a), and he undoubtedly had a right to spread the pay he received for those services, if, and, when he received it. Now, Section 1301 was enacted in 1954.

We quote from 82 Corpus Juris Secundum, page 994:

> "Retroactive legislation changing rights is not favored, and the rule that statutes are not to be construed retrospectively unless such construction was plainly intended by the legislature applies with peculiar force. Hence, in so far as affecting vested rights, a statute will be construed as prospective only, and not as operating retrospectively or retroactively, unless that intention is made manifest either by express words or by a clear, distinct, necessary, plain, strong or unmistakable, implication."

Again, quoting from 82 Corpus Juris Secundum, page 845:

> "In the absence of definite indication of a legislative purpose to that end, the re-enactment of a statute does not affect its meaning or enlarge its scope, and is not regarded as a new enactment but a continuation of the language repeated; nor does mere change in language necessarily indicate an intention to change the law."

As supporting the quotations from Corpus Juris Secundum, we call the Court's attention to the case of *New York Life Ins. Co.* v. *Truesdale,* (4th Cir.) 79 F.2d 481, from which we quote:

> "In addition to this, it is a well-settled rule of construction that statutes effecting a change in substantive rights will not be given a retroactive effect unless it clearly appears, which is not the case here, that the Legislature so intended. Even statutes modifying statutes of limitations will not be construed as having the effect of reviving a cause of action already barred, if such construction can reasonably be avoided."

II

(Liquidating Dividends on Stock Constitute a Sale)

The question in this Second Division would appear to be very simple, and we quote the statement from the Circuit Court Opinion, last paragraph, page 11:

> "For present purposes we may assume, as did the Tax Court, that the certificates were capital assets under Sec. 1221's general definition of 'property held by the taxpayer'. And they were held by this taxpayer more than six months. The inquiry then is only whether the gain resulted from a 'sale or exchange'. This, of course, is essential if it is to qualify as long term capital gain. Dobson v. Commissioner, 321 U.S. 231, 232 (1944); Commissioner v. Gillette Motor Transport, Inc., 364 U.S. 130, 133 (1960)."

That left but one question. If the taxpayer could show a "sale or exchange", he was entitled to long-term capital gain, and it is elementary, of course, that the words "sale or exchange" do not carry the meaning usually given to them in everyday conversation.

The taxpayer's conclusions were very simple. He had two trust certificates. Exhibit 10 recited that he owned

.4666 percentage of the stock held by the trust, and Exhibit 14 recited that he owned .0388 percentage, so on both certificates he owned a trifle over 50% of the stock held by the trustee, and the trustee held 500 shares of Urbandale stock. The Urbandale company was completely liquidated in 1955 by a sale of its one asset, to wit, an interest in 220 acres of land. The money was paid by Urbandale as liquidating dividends to the trustee, and the trustee a few days later passed the money on to the owners of said stock. The trust was liquidated, and the stock was cancelled.

The taxpayer made his returns on the assumption that he had a long-term capital gain of something over $9,000, as he had owned stock that was liquidated by the complete liquidation of the corporation, which in fact was equivalent to a *sale*, in fact this operation is pretty much in the nature of a forced *sale* similar to the procedure in condemnation, but it is rather pointless to discuss the nature of "liquidating dividends" and why they constituted a "sale", because Section 302 of the 1954 Code, and likewise Section 331 (1954) Code, both recite that these dividends in liquidation "shall be treated as a distribution in part or full payment in *exchange* for the stock". (Our emphasis).

Again, looking at this matter from another angle, at the time that this Urbandale company was liquidated, this trustee had nothing of any value except 500 shares of Urbandale stock, and it received in liquidating dividends approximately $40,000, which was the net amount left from the sale of the land, and was paid in complete liquidation of the stock, so the trustee returned the stock to the erstwhile officers of the company, and it was cancelled (Ex. 6-Final Report of Trustee). We assume nobody could deny that the money received by the trustee in liquidation of all of its stock was described as liquidating dividends, and constituted a "sale" of the stock.

Again, these "liquidating dividends", when passed on to the six beneficiaries, retained the "same character in the hands of the beneficiary as in the hands of the trust". Consequently the money that passed on to this taxpayer from the trustee was identified as liquidating dividends in payment for his interest in the 500 shares of stock held by the trustee, and as such it was a "sale or exchange" and, as hereinbefore set out, this taxpayer has nothing more to prove except the "sale or exchange" as the other elements of the problem were conceded. That is what he thought.

As supporting the foregoing conclusion, which is more or less elementary, we call the Court's attention to Rev. Rul. 56-78, C.B. 1956-1, 648, also described as No. 6269 Rev. Rul. 56-78, I.R.B. 1956, 1027, and reference is made to Sec. 162 (b) of the 1939 Code (now identified as Sections 651-652, 661 and 662 of the 1954 Code).

> "Capital gains realized by the trustee from the sale of trust property, which are distributed to the beneficiaries under the provisions of 162 (b) of the 1939 Code, would also be capital gains in the hands of the certificate holders."

No criticism was made of this Urbandale situation until the matter reached the "Accounting Office" (or Appellate Division) in Omaha, and the Deficiency Notice ultimately filed by the so-called Appellate Division, and identified herein as Exhibit C in Schedule 2-Par. (d), determined that the gain was "ordinary income", because it was realized from the "liquidation of trustee's notes rather than * * * received in liquidation of corporation stock". Again, in Exhibit C, Schedule 5, Par. (b), this same finding was repeated by the Appellate Division; that is, the liquidating dividends of the Urbandale corporation were said to be payments on "trustee's notes", and therefore there was no "sale or exchange".

Again, when this question reached the Tax Court, T.C.Memo 1962-230, the Tax Court followed the Appellate Division, and held no long-term capital gain established, because there was *no sale or exchange,* and there was no sale or exchange because the *liquidating dividends* were applied to "trustee's notes". (Appendix "C", pp. 19-20).

No explanation appeared in either Exhibit C (Deficiency Notice) or the Tax Court Memo 1962-230, indicating why Exhibits 10 and 14 were "trustee's notes", as obviously there was no promise to pay any amount, at any time, at any place. Again, the trustee that signed Exhibits 10 and 14, to wit, the First State Bank & Trust Company, on the 17th of February, 1931, obviously could not, and would not, under any circumstances have executed a note or "evidence of indebtedness" in executing Exhibits 10 and 14 (and also the other four trust certificates). In fact, said trustee followed out the very specific provisions of Exhibit 5 (p. 10, last 4 lines) in the Trust Agreement:

> "said trustee to be authorized to execute any *appropriate pledge* to assure said creditors that said corporate stocks are held by said trustee as security for their benefit pro rata of said several creditors." (Our emphasis).

For reasons that we assume are obvious, the Circuit Court could not very well go along with the Tax Court's idea about "trustee's notes", but we really can't feel that the situation has improved much, if any, as the C.C. Opinion described the six certificate holders as "claimants against the trustee". In rather a broad sense we assume that this is true, but not in the way the Court had in mind. because every stockholder would *in a sense* be a claimant even as against the corporation which issued the stock.

Nevertheless under the Federal Statutes, and particularly Code Section 302 (a) and Sub-Sec. 3 of the 1954 Code, and Code Section 331 of the 1954 Code, *liquidating dividends* paid on corporation stock constitute a "sale or exchange" even though the stockholder could be considered to be a "claimant" in a broad sense, a *very broad sense.*

Again, the Circuit Court had to find that the six claimants did not release their claims in Exhibit 5, although Paragraph 7, page 5 of said exhibit, stated:

> "The following claims of the undersigned creditors against said estate of W. N. Merritt shall be satisfied and released by payment as part of the purchase price of the property to be so purchased from said executor with interest computed to September 1, 1930, to wit."

All six claimants signed, the executor and the estate beneficiaries signed, but the Opinion states on page 14, last line:

> "This, however, we do not construe and interpret as effecting a novation or basic change in the posture of the six creditors and their successors. Their interests were still in the nature of claims definite in amount and with a specified interest rate. Instead of being applicable to all the assets of the decedent's estate, these became confined to those fewer assets which had come from the estate to the trustee by way of the 'purchase' and pursuant to the understanding reached by all concerned. The release of the claims therefore had significance only as it freed untransferred assets of the estate from the claims of the six major creditors. These creditors' claims were still directed to the transferred assets."

Let's look at the Court's ruling a minute. He says that these six hard pressed creditors of what looked like an insolvent estate, five women, mostly on the elderly side, and one insolvent bank, were, in fact, in Exhibit 5, entering

into an agreement to release from their respective and fair liens *all of the assets in the estate* except this Des Moines property.

According to the Court this benevolent, charitable group of creditors were going to give up their claims to all of the assets and settle for a few of the "transferred assets". There is absolutely nothing to support this rather far fetched idea, because the claims were absolutely released in every respect. The so-called "transferred assets" were sold and delivered to the creditors, or to a trustee selected by them, for the sum of $27,500. The trustee forthwith deeded the so-called "transferred assets" immediately to the Urbandale company.

Again, in connection with this unique, but rather difficult to prove, theory that the Circuit Court adopted, that these instruments, Exhibits 10 and 14, were in fact "partial claims" against part of the assets of the Merritt estate, or against the trustee, we do not know which, we call your Honor's attention to the agreed Stipulation of Facts, and particularly Item 13, which reads:

> "Attached hereto, and marked Exhibit 10, is a photostatic copy of a Trust Certificate issued on February 17, 1931, by the First State Bank & Trust Company of Fort Dodge, Iowa, as Trustee, to the First National Bank of Fort Dodge, Iowa, in exchange for its claim against the Estate of W. N. Merritt, deceased."

Apparently when we drew the Stipulation of Facts, we were dealing in whole claims and not *partial* claims.

Again, the Circuit Court was confronted with the language of the certificates, see Exhibits 10 and 14. The Opinion says with reference to this (Opinion, p. 12, last paragraph):

"That they were exactly that is a result which seems to us to be unavoidable. It is true that each certificate recites that the holder 'is the owner of (a stated percentage) of the equitable ownership and beneficial interest in' named stocks, including Urbandale, 'title to which' is held by the trustee, 'for the benefit of the holder'. *But labels do not determine ultimate character.*" (Our emphasis).

We believe that the last line is more or less indicative of the Court's reasoning as a whole with reference to the certificates.

Again, the Court was confronted by the quit claim deed executed by the beneficiaries of the Merritt trust in 1952, and the Opinion says:

(Opinion page 15) "Neither do we regard as opposingly significant the quit claim deed executed by the will beneficiaries in 1952, before the taxpayer's acquisition of the two certificates in 1954 but after the coal mining operations had ceased. *Its apparent purpose, it seems to us, was that of title clarification.*" (Our emphasis).

The Court does not explain that the complete (undisputed) record shows these payments in 1955 and 1956 were all liquidating dividends. No attempt is made to circumvent this, that is, the Urbandale land was sold and the net proceeds were paid on the stock to liquidate it, and one-half of the money went to Kelleher and one-half to the trustee. The trustee held one-half of the stock, and Kelleher owned the other one-half of the stock. Liquidating dividends as to both halves constituted a "forced sale". Any stockholder, who owns stock in any corporation, and the directors decide to liquidate the company, the stockholder is necessarily a "seller" on a "forced sale", and one-half of this money went to the trustee as liquidating dividends. Obviously, it was a "sale" and in this case

"capital gain" as opposed to the dividends that were paid out on coal royalty for seventeen years, as said coal royalty dividends were ordinary income, both to the trustee and the actual owners of the stock, which were the six certificate owners. As shown by the record (Ex. 6, p 13, Par. 2) the Urbandale stock, which was held by the trustee, was all liquidated and returned to the erstwhile officers of the company (Ex. 6-Final Rep. of Trustee).

It is rather interesting to note that this liquidation of Urbandale, which amounted to approximately $80,000 went one-half to Kelleher and one-half to The State Bank, as trustee, for these six people who owned the stock. Obviously, on Kelleher's one-half, he made money between what the stock cost him in '31 as against the liquidating dividends of $40,000 in 1955-1956. No one, I think, could deny that *it was a long-term capital gain.* The trustee sits in exactly the same position with the same number of years and the same number of shares. Obviously, it is long-term capital gain to the trustee just as it is to Kelleher, and whatever its character is as to the trustee, it maintains the same character, to the taxpayer, as the trustee was nothing more than an agent for the six owners of 500 shares of this stock of Urbandale. What is capital gain for Kelleher is capital gain for them.

The Court attempted, at least, to assume that the quit claim deed, Exhibit 21, had some motive or ulterior purpose not disclosed by the record at all, when he said on page 15 of the Opinion:

> "Its apparent purpose, it seems to us, was that of title clarification."

There is nothing to support, or even suggest this supposition, and he goes on further in the same paragraph by saying:

> "Had the deed been intended to operate as a release of the will beneficiaries' interests under the agreement, it is reasonable to suppose that broader provisions to that effect would have been forthcoming."

The Record shows at page 30 of the Transcript the rights of the beneficiaries under Exhibit 5, page 5, Par. 5, were being discussed by counsel for the government, and the said government attorney was inquiring (Trial before Tax Court) of the taxpayer on cross-examination as to whether or not *he* drew said Exhibit 5, and the taxpayer answered (Trans. p. 30, l. 23):

> "That's right. I drew that, but the land was deeded outright in '52. Eventually to avoid any question about the thing, the heirs signed a 'quit claim deed'."

Continuing on page 31, line 1: Commissioner's attorney cross-examining taxpayer:

> "Q. Now, then, they also in consideration of that release their rights in that trust agreement; Is that correct?
>
> A. That's correct.
>
> Q. It is signed by Margaret Merritt, Doris Olney Merritt, guardian for William O. Merritt, Allen Merritt and Floyd Merritt, minors, beneficiaries under the will of W. N. Merritt, and by Maurice J. Breen. They released their rights in the property to the trust?
>
> A. That's right. There is the deed. I said '52; that's right '52."

It is a little bit difficult to rechristen and completely reverse the import of several of these key exhibits, to wit, the release of the claims in Exhibit 5, the *very* essence of the trust certificates, Exhibits 10 and 14, and the record on the *sale* and *deed* by the estate to the Trustee, the *deed* by the Bank, as Trustee, to the Urbandale Company (Trans. p. 10, l. 7), the fact that the Trustee was the agent of the

six creditors (Trans. p. 10, l. 9), and again the quit claim deed (Ex. 21) in 1952. There is nothing to support the Court in this position, except his desire not to believe what he sees.

It may be assumed that the only question in this division, at least as looked upon by the Circuit Court, was whether or not this was a "sale or exchange". This is stated at the top of page 12 of the Opinion. The Court then in the next succeeding paragraph (page 12, Par. 2) says:

> "It is well established that, apart from the existence of a qualifying definition, payments made upon an obligation do not constitute a sale or exchange. Fairbanks v. United States, 306 U.S. 436, 437 (1939); Graham v. Commissioner, 304 F.2d 707, 708 (2 Cir. 1962); see Paine v. Commissioner, 236 F.2d 398 (8 Cir. 1956). Just such a special definition is contained in Sec. 1232 (a) (1) with respect to certain evidences of indebtedness."

We take it by this paragraph above stated that the Court held that Exhibits 10 and 14 were "obligations" rather than *certificates of partial ownership* in the Urbandale stock held by the trustee. That is the essence of this controversy. The Court says that these two exhibits were "obligations". The word itself without any amplification does not mean much, I suppose, other than to classify it, as being something related to a note or bond, or again as a "partial claim" against "transferred assets" in the hands of the trustee.

This whole deal about the "partial claim" and the "transferred assets" is rather novel, and certainly there is nothing in the record that supports it; in fact, irrespective of the record, or this case in particular, I would assume that the whole idea was pretty much new and untried.

Apparently the certificates, according to the Court, *must be "obligations"*, rather than fractional interests in corporation stock, as that is what each instrument said it was, a fractional interest in the ownership of Urbandale stock.

Again, going back to the Court, he must have thought that it was obvious that these certificates were *not* "trustee's notes", as held by the Tax Court, so he called them "partial claims"; in other words, the First National Bank signed Exhibit 5, and released its claim against the Merritt estate *in full*, again released its claim on the probate records, and in consideration of that *complete* release entered into this purchase agreement for the Merritt land for $27,500, the *total amount* of the six claims, and secured a deed from the Merritt estate to the trustee *selected by the six creditors, as their agent*, to hold this land (and the stock was subsequently issued in place of the land) *for the six creditors.* The Bank (First National) really had not done these things at all *according to the Court.* It actually did not release its claim against the estate. The Court said that it merely released *some of the assets of the estate*, and again it did not *buy* the Des Moines coal property at all; in fact, according to the Court, when the deal was finished, the First National Bank had not released its claim. It had merely limited its lien, under its claim against the estate, to this stock, and the *estate* owned the stock (not the six creditors) in the name of the trustee. When the stock was liquidated, the *liquidating dividends* were paid. They were paid to this taxpayer not as a stockholder, but as a "partial claimant" against the Merritt estate, that is the Circuit Court's version of this question.

To go along with this notion that Exhibits 10 and 14 are "partial claims", you must deny in every respect that these claims in 1930 and 1931 were absolutely released

and satisfied, as to this estate, you must deny in consideration thereof ($27,500) the estate deeded this Des Moines property to the trustee, who was nothing more than an agent or assignee for the six creditors. (Trans. p. 10, l. 9). They bought the land for the claims. They selected the Bank as their agent, and it in turn, that is, the bank trustee, took title to the Urbandale stock *for the six creditors* (Trans. p. 10, l. 9), that is the whole case, and that has to be denied *in its entirety* in order to convert Exhibits 10 and 14 into "partial claims", and again to convert the Des Moines property, which was bought and paid for, which was deeded and redeeded twice afterwards into "transferred assets", or an unsold part of the *estate assets,* to a trustee.

The Court in the vital paragraph, which we quoted on Page 12 of the Opinion, cites three cases, which one would assume must support his theory, but not one of the cases has the *slightest* relation to his idea.

The *Fairbanks* case (*Fairbanks* v. *United States,* 306 U.S. 436, 437) involves nothing but conventional corporate *bonds* that were redeemed before maturity, and under ordinary circumstances a bond is an obligation. It is not stock, and has no relation at all to Sections 302 and 331 of the 1954 Code, which specifically provide for the liquidation of *corporate stocks*—not bonds.

Again, the second case cited, which is *Graham* v. *Commissioner,* 304 F.2d 707, 708 (2 Cir. 1962), involves German *bonds* given in settlement of war debts. Apparently the bonds were bought for $10 a bond and ultimately the buyer received $2,000. These again are *bonds,* and have no relationship to this case on trial *whatsoever.*

The third case that the Court cites is *Paine* v. *Commissioner,* 236 F.2d 398 (8 Cir. 1956). The obligations involved in this case were *serial promissory notes* coming

due over a period of years, given as part of the purchase price of some Minnesota land, or mineral rights.

It must have been obvious to the Court that these two bond cases, and one promissory note case had nothing to do with the case at bar, because every one connected with the case, who is familiar with it at all, knows that a bond, or a note, is an *obligation*, and that liquidating payments on it, a bond or a note, are *not capital gain but ordinary income*. Moreover the Court must have known that these three cases did not sustain, or even relate to, his notion that Exhibits 10 and 14 were "partial claims" against "transferred assets". And said Court well knew that the liquidating dividends of the Urbandale company paid in 1955-1956 were paid to this taxpayer as the owner of a trifle more than 50% of the Urbandale *stock* in the hands of the trustee, which in fact amounted on the whole to a trifle *over 25% of the total stock in the Urbandale company.*

Under Code Sections 302, 331, 652 and 662 of the 1954 Code these liquidating dividends, that came into the hands of the trustee, represented and constituted a "sale or exchange" of the stock, all these funds continued to be the proceeds of a "sale or exchange" when immediately transferred to the beneficial owner of the stock, to wit, this taxpayer.

CONCLUSION.

The Circuit Court Opinion is beautifully written from a rhetorical viewpoint, and it certainly evidences an unusual familiarity with the facts, and again the handling of Division II, so as to eliminate the "Trustee's notes" theory of the Tax Court, and substitute one that surely was new and unique but, as far as we can see just as fallacious and unsupported as the "Trustee's Notes" idea, took unusual

work, or ability, or probably both, because, if one were not too familiar with the situation, and the peculiarities of the Statutes dealing with the matter of liquidating dividends as applied to corporation stock and corporation held by the trustee, it could be, and was, most readable and convincing.

We ask that this Petition be granted, because the Opinion sets up an entirely new interpretation of the Statutes in reference to the "spreading of fees for personal services", and is in direct conflict with a similar Opinion in the Second Circuit.

Again, this Opinion ignores the statutes relating to corporate liquidating dividend as constituting a "sale or exchange" of *stocks*, and this obviously is most important where the rules in reference to "capital gain" are so vital to the American taxpayer, and that is particularly true with reference to corporation stocks, as a common type of investment.

Respectfully submitted,

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APPENDIX A

United States Court of Appeals

FOR THE EIGHTH CIRCUIT

No. 17,308

Maurice J. Breen and Alyce Breen, *Petitioners,* v. Commissioner of Internal Revenue, *Respondent.*	On Petition for Review of the Decision of the Tax Court of the United States.

(February 26, 1964.)

Before VAN OOSTERHOUT and BLACKMUN, Circuit Judges, and HANSON, District Judge.

BLACKMUN, Circuit Judge.

Maurice J. Breen, a cash basis taxpayer, and his wife, have petitioned for review of the Tax Court's determination of deficiencies in their federal income taxes for the calendar years 1955 and 1956. Four issues were presented to the Tax Court. Two were decided adversely to the taxpayer and are here before us. The other two were decided largely in the taxpayer's favor. Judge Mulroney's opinion, not reviewed by the entire court, is T.C. Memo 1962-230. The Commissioner filed a cross-petition for review but it has been dismissed by this court on stipulation of the parties. Commissioner v. Breen, 316 F.2d 735 (8 Cir. 1963).

The issues are:

1. Whether the taxpayer was entitled, with respect to a $4,200 fee received in 1955, to the benefit of the spreading provisions of Sec. 1301 of the Internal Revenue Code of 1954, 26 U.S.C.A. Sec. 1301.

2. Whether gains the taxpayer realized in 1955 and 1956 on two trustee's certificates were ordinary income or were long term capital gain under Sec. 1222 (3), 26 U.S.C.A. Sec. 1222 (3).

The facts, most of them stipulated, are not in dispute; W. N. Merritt died in May 1928. Among his assets at his death were undivided interests in two tracts of real estate near Des Moines in Polk County, Iowa. These were heavily mortgaged. The taxpayer, a practicing lawyer, was named as executor and trustee in the decedent's will.

The assets of Merritt's estate were insufficient to meet the claims of creditors. In September 1930, a "Trust Agreement and Appointment of Attorney in Fact" was executed by the six major creditors, whose claims aggregated about $27,500, and the will beneficiaries and with a bank as trustee. This agreement provided that (a) the six creditors released their claims against the estate; (b) the trustee assumed the title to the decedent's interests in the Polk County real estate and to certain stock not significant here; (c) the release of the claims was the purchase price for that property; (d) the trustee was authorized to convey the real estate interests so received to Urbandale Coal and Acreage Company, a newly organized Iowa corporation, in exchange for half its stock; (e) the trustee was to hold that stock as trust property "and as security for notes evidencing the * * * indebtedness" to the creditors and to apply income of the trust in payment of interest and principal; (f) Urbandale was to receive, in exchange for the other

half of its stock, equal undivided interests owned by attorney D. M. Kelleher in the same real estate; and (g) the trustee was to hold the trust property until the indebtedness to creditors and the interest thereon were "paid in full, and thereafter hold the same for distribution to * * * the beneficiaries under the will of said W. N. Merritt in the proportions they are entitled to share in the Estate of said Testator".[1]

The trustee issued a certificate to each of the six creditors. This recited that the creditor was the owner of a stated percentage "of the equitable ownership and beneficial interest in" the stock, including preferred and common of Urbandale, held by the trustee "for the benefit of the holder or holders of this certificate and all similar certificates issued"; that "when said interest and principal have been paid in full through the disbursements of said trustee, then this certificate shall have no more value"; and that the certificate "may be assigned and transferred".

Almost 24 years later, in April 1954, the taxpayer purchased for $2.500 a trustee's certificate representing a 46.66% interest in the trust and an original creditor's claim of $12,923.92. A week later the taxpayer purchased for $150 a second certificate representing a 3.84% interest and a creditor's claim of $1,050.

Meanwhile, through a working mining company, Urbandale operated the coal mine on the Polk County land on a royalty basis until 1947. In December 1952 the Merritt estate beneficiaries gave Urbandale a quit-claim deed to the land.

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1. Apparently there were other assets of the Merritt estate which were not so transferred to the bank as trustee; these, instead, were retained by Breen as the fiduciary under the Merritt will. He received fees for his services in that capacity, but that remuneration is not now claimed to have significance.

During this entire period the taxpayer was president of Urbandale, Kelleher was vice-president, and Mrs. Kelleher was secretary-treasurer. These three also comprised the directorship of the corporation during its corporate life.

When the mining operations ceased, the taxpayer, as president of Urbandale, began to negotiate for the sale of the land. This pursuit proved successful and late in 1954 the land was sold. Urbandale then adopted a resolution to liquidate. In March 1955 Urbandale's shareholders approved payment of a $4,200 fee to the taxpayer and of a like fee to Mrs. Kelleher. The authorizing resolution stated that, throughout its corporate existence of more than 24 years, no compensation had ever been paid to any officer or director, and

> "(1) That the said Maurice J. Breen and Mary S. Kelleher, each, be allowed the sum of $200.00 a year for their services as directors, and their services in attending board meetings and committee meetings, and other incidental work connected with the management of said corporation.
>
> "(a) That said allowance extend over the first twenty-one years of the life of this corporation, as said twenty-one years covers the active operation of this corporation while it was engaged in the production of coal, and that said allowance to each of said named directors, to wit, Mary S. Kelleher and Maurice J. Breen, be in the sum of $4200.00 each."

The taxpayer's $4,200 fee was paid in 1955. Except for a $500 fee paid in December 1949 for legal services on a special matter, the taxpayer had received no other compensation from Urbandale.

The trustee, from 1931 through 1956, made payments to the certificate holders. These were distributions from the coal royalties and upon the liquidation. Breen received approximately $8,250 in 1955 and $13,350 in 1956 upon the two certificates he had purchased in 1954. He thereby realized gain.

1. The $4,200 payment. In his 1955 return the taxpayer claimed the benefit of Sec. 1301 for this fee. The Commission ruled otherwise.

The taxpayer's argument here is that depression conditions prevailed after the inception of the Merritt estate; that the real estate, because of its location near Des Moines, had subdivision potential; that the coal royalties were intended to provide for the payment of interest, taxes, and mortgage requirements until the land could be sold advantageously; that sale of the land at a proper price was the desire of the taxpayer and Kelleher and the creditors; that the taxpayer acted as president, director, and liquidating agent of Urbandale but until 1954 had no ownership interest of any kind in that corporation; that his only purpose was to handle Urbandale so that the land could be liquidated for the certificate holders; that his duties were not those of a managing officer of a conventional corporation but were directed, instead, to working out the sale; that there are many cases under the 1939 Code which apply the statutory benefit to payments received for corporate management; and that Sec. 1301 in this respect effected no change in the prior law.

This argument has some appeal but it is not sufficient. Furthermore, the record does not fully support it.

Those portions of Sec. 1301 which are pertinent here are set forth in the margin.[2] The section's predecessor was Sec. 107 (a) of the 1939 Code, as amended.[3] The statute originally appeared in Sec. 220 (a) of the Revenue Act of 1939; this was amended by Sec. 139 (a) of the 1942 Act. These pre-1954 forms of the statute all referred to compensation "for personal services" and were not embellished with the "an employment" and the "to effect a particular result" language of the 1954 version. It is

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2. Sec. 1301. "(a) Limitation on tax.—If an individual * * *

(1) engages in an employment as defined in Subsection (b); and

(2) the employment covers a period of 36 months or more * * * and

(3) the gross compensation from the employment received or accrued in the taxable year of the individual * * * is not less than 80 percent of the total compensation from such employment, then the tax attributable to any part of the compensation which is included in the gross income of any individual shall not be greater than the aggregate of the taxes attributable to such part had it been included in the gross income of such individual ratably over that part of the period which precedes the date of such receipt or accrual.

"(b) Definition of an employment.—For purposes of this section, the term 'an employment' means an arrangement or series of arrangements for the performance of personal services by an individual * * * to effect a particular result, regardless of the number of sources from which compensation therefor is obtained."

3. Sec. 107. "(a) Personal services. If at least 80 per centum of the total compensation for personal services covering a period of thirty-six calendar months or more (from the beginning to the completion of such services) is received or accrued in one taxable year by an individual * * *, the tax attributable to any part thereof which is included in the gross income of any individual shall not be greater than the aggregate of the taxes attributable to such part had it been included in the gross income of such individual ratably over that part of the period which precedes the date of such receipt or accrual."

said that the 1954 change was made to express more accurately the intended meaning and to eliminate tendencies to combine or to separate services as suited one's tax convenience. Senate Report No. 1622, 83d Cong., 2d Sess., pp. 445-46; House Report No. 1337, 83d Cong., 2d Sess., p. A289. Only in this narrow sense of clarifying "the intended meaning" is the taxpayer correct in saying that the 1954 Code did not change the earlier statute. See *Wattley* v. *Commissioner*, 275 F.2d 461, 464 (2 Cir. 1960), cert. denied 364 U.S. 864.

There is a suggestion in the taxpayer's brief that, because the fee was for services rendered in calendar years prior to 1954, it is the 1939 Code, rather than the 1954 Code, which applies. We cannot agree. The fee was paid in 1955 to this cash basis taxpayer. The 1954 Code, accordingly, controls. This result seems obvious from the very language of the Code and from its Sec. 7851 (a)(1)(A). See *United States* v. *Whitney Land Co.*, 324 F.2d 33 (8 Cir. 1963) and *McClure* v. *United States*, 228 F.2d 322, 324 (4 Cir. 1955). We note that in at least one other case this conclusion has been taken for granted, even though part of the earnings period preceded the effective date of the 1954 Code. *Frank Stephen Ranz*, 31 T.C. 91 (1958), affirmed, *Ranz* v. *Commissioner*, 273 F.2d 810 (6 Cir. 1960).

The purpose of Sec. 1301 and its predecessors was obviously to grant relief, apparently at the option of the taxpayer, *United States* v. *Behle*, 316 F.2d 134, 135 (10 Cir. 1963); *Guy C. Myers*, 12 T.C. 648 (1949), from tax hardship otherwise resulting upon the bunching of income received for personal services rendered over a long period of time. *Chase* v. *Commissioner*, 245 F.2d 288, 290 (9 Cir. 1957); *Van Hook* v. *United States*, 204 F.2d 25, 27 (7 Cir. 1953), cert. denied 346 U.S. 825; Senate Report No. 648, 76th Cong., 1st Sess., p. 7; 1939- 2 C.B. 524, 528-29. But,

being a relief statute, it is to be given "close scrutiny" and is not entitled to a liberal interpretation. *Smart* v. *Commissioner*, 152 F.2d 333, 335 (2 Cir. 1945), cert. denied 327 U.S. 804; *Ranz* v. *Commissioner, supra*, p. 813 of 273 F.2d; *Zillmer* v. *United States*, 233 F.2d 912, 914 (7 Cir. 1956); *Faul* v. *Commissioner*, 263 F.2d 645, 650 (9 Cir. 1959); see *Wattley* v. *Commissioner, supra*, p. 465 of 275 F.2d, and *Helvering* v. *Northwest Steel Rolling Mills, Inc.*, 311 U.S. 46, 49 (1940); cf. *Slough* v. *Commissioner*, 147 F.2d 836, 839 (6 Cir. 1945). The burden is on the taxpayer to show that he comes within the favor of the statute. *Reynolds* v. *Commissioner*, 249 F.2d 259, 261 (4 Cir. 1957); *Van Hook* v. *United States, supra*, p. 28 of 204 F.2d, *Sloane* v. *Commissioner*, 188 F.2d 254, 261 (6 Cir. 1951); *Lindstrom* v. *Commissioner*, 149 F.2d 344, 346 (9 Cir. 1945); *United States* v. *Robertson*, 190 F.2d 680, 683 (10 Cir. 1951), affirmed, 343 U.S. 711.

There is no question here about the satisfaction of the 36 month and 80% requirements of the statute or about the fee's being a payment for personal services. The question thus is the narrow one whether Mr. Breen's personal services qualify as "an employment * * * to effect a particular result".

We, as did the Tax Court, conclude that the answer to this question is in the negative. We do so because of several factors. First, the Urbandale resolution is almost conclusively destructive of the taxpayer's position. The $200 a year compensation is described as payment for "services as directors" and for attending meetings and for "other incidental work connected with the management". The 21 year period is said to cover the active operation of the corporation "while it was engaged in the production of coal". Breen himself voted in the affirmative for this resolution. Whether or not, as the taxpayer speculates in

his brief, the language was that of Mr. Kelleher and was drawn in the light of Kelleher's own social security situation, we do not know. We must take the record as we find it. When we do so, the resolution's language rings with the tone of general services and not at all with that "to effect a particular result". Second, the resolution reveals nothing by way of recognition of a primary purpose in the taxpayer's employment. Third, the trustee's final court report recites that "shortly after the coal ceased to be mined" the taxpayer "began negotiations with various prospects to sell all, or a substantial portion, of said land". This indicates that the real effort for the sale came only from 1947 on, after the mining ceased to be productive and had ended and when the bulk of the 21 year period had already elapsed. Fourth, no explanation is offered as to the nature of Mrs. Kelleher's fee. This paves the way for an inference that the fees were divided equally between Mr. Breen, as representative of the certificate holders, and Kelleher, as the owner of the other half of the trust's beneficial interests. All this provides a sufficient and appropriate basis for the Tax Court's finding and conclusion that the taxpayer's services were not "an employment" within Sec. 1301 (b) of the 1954 Code.

What few authorities there are lend support to this result. Regs., Sec. 1.1301-2 (b)(1)(i) and (ii) and 2(b)(2), Example (1), illustrate the denial of the statutory benefit for "general services" and make the facts of each case govern its disposition. *Ranz v. Commissioner*, *supra*, 273 F.2d 810 (6 Cir. 1960), concerned commissions received by a sales agent in 1954. His contract of employment was to sell equipment. His intensive work over several years resulted in orders from Ford Motor Co. The Sixth Circuit observed, p. 812 of 273 F.2d, that the agreement "appears to be free from ambiguity and contains no terms or pro-

visions from which it could be concluded that it was the purpose of the parties to particularize its objects and purposes in the manner insisted upon by petitioner. On the contrary * * * it is clear that its purpose was to employ the petitioner as a general sales representative in his area * * *. It was not an agreement to sell to Ford alone * * *." The Tax Court's refusal to apply the statute was accordingly affirmed.

Wattley v. *Commissioner, supra*, 275 F.2d 461 (2 Cir. 1960), does not give the taxpayer the support he claims. That taxpayer was a real estate broker. Over a period of years he attempted to obtain a lease on certain New York City property. His effort finally proved successful and in 1951 he received his commission. The 1939 Code was thus applicable. The court did observe, p. 464 of 275 F.2d, with respect to the 1954 Code, that "it appears that the Congress did not suppose that it was changing the meaning of Sec. 107 (a) when it was enacting Sec. 1301 in its present form", but this comment is obviously concerned with the statute's basic purpose which we have already noted above. The facts of Wattley, it seems to us, are those of a broker's efforts to obtain a lease for a specific piece of property. His work was directly concerned with the renting of that real estate. His activity was "to effect a particular result".

Wattley would support the taxpayer's position here were his employment made, as he contends, only to effect the sale of the Polk County real estate. But his activities were broader than that. He was a director and an officer and the management force behind Urbandale. He was responsible for its coal royalties. His services were all incidental to his various corporate capacities and responsibilities. While sale may have been the ultimate objective, his activities were not confined to that target. See *Reyn-*

olds v. *Commissioner*, *supra*, 249 F.2d 259, 261. Whatever the result might have been under Sec. 107 (a) of the 1939 Code, which we do not pass upon, his position is defeated by the restrictions of the 1954 Code.

2. The receipts from the trust certificates. The taxpayer reported his gain upon these receipts as long term capital gain. The Commissioner ruled that it was ordinary income.

The taxpayer's approach is that his acquisition of the two certificates gave him an "interest in the Urbandale corporation stock"; that Urbandale made distributions in liquidation or redemption of its stock which, by Sec. 331 (a) (1) or by Sec. 302 (a) and (b) (3), are to be treated as in "full payment in exchange for the stock"; that the claims against the estate were discharged in 1930; that the estate's interest in the land was sold for the amount of the six claims; that the certificates themselves recited that the holder is an owner of a stated percentage of the Urbandale and other stock; that the references to "notes" and the like which crept into the papers were loose language used long ago; that the trustee had no authority to issue a note or evidence of indebtedness; that each former claimant's position, with the 6% provision, was similar to that of a holder of preferred stock; that the will beneficiaries were like common shareholders; and that the certificates were pledges and not notes because no one agreed to pay a specific sum at any time to anyone and no one agreed that he was indebted to the former creditors.

Viewing the case upon its particular facts, *Frank* v. *Commissioner*, 321 F.2d 143, 148 (8 Cir. 1963), we think the result reached by the Tax Court on this issue was also correct.

For present purposes we may assume, as did the Tax Court, that the certificates were capital assets under Sec. 1221's general definition of "property held by the taxpayer". And they were held by this taxpayer more than six months. The inquiry then is only whether the gain resulted from a "sale or exchange". This, of course, is essential if it is to qualify as long term capital gain. *Dobson* v. *Commissioner*, 321 U.S. 231, 232 (1944); *Commissioner* v. *Gillette Motor Transport, Inc.*, 364 U.S. 130, 133 (1960).

It is well established that, apart from the existence of a qualifying definition, payments made upon an obligation do not constitute a sale or exchange. *Fairbanks* v. *United States*, 306 U.S. 436, 437 (1939); *Graham* v. *Commissioner*, 304 F.2d 707, 708 (2 Cir. 1962); see *Paine* v. *Commissioner*, 236 F.2d 398 (8 Cir. 1956).. Just such a special definition is contained in Sec. 1232 (a) (1) with respect to certain evidences of indebtedness. Section 1232 first appeared as Sec. 117 (f) of the Revenue Act of 1934 and was intended to "take out of the bad debt provision certain transactions and to place them in the category of capital gains and losses", *McClain* v. *Commissioner*, 311 U.S. 527, 529 (1941). No alternative contention, however, is made by this taxpayer that Sec. 1232 has any application to these certificates and, indeed, we do not see how it could be made in view of the statute's language.

No other statute which would define the transaction before us as a sale or exchange is suggested. As a consequence, Fairbanks and the cases which follow it control the present situation if the distributions to the taxpayer were payments upon an obligation.

That they were exactly that is a result which seems to us to be unavoidable. It is true that each certificate recites that the holder "is the owner of (a stated percentage) of the

equitable ownership and beneficial interest in" named stocks, including Urbandale, "title to which" is held by the trustee "for the benefit of the holder". But labels do not determine ultimate character, *Carlberg* v. *United States*, 281 F.2d 507, 514 (8 Cir. 1960). Other characteristics of the certificates and the contents of other pertinent documents readily convince us that the agreement-certificate-trustee arrangement was simply one for the benefit of the six creditors concerned and was in the nature of an assignment for the benefit of those creditors. We are impressed in this connection with the following: (a) The agreement's provisions that the trustee is to hold the Urbandale stock "as trust property and as security for notes evidencing the amount of present indebtedness of creditors of said estate" and "as security for the claims of said above described creditors until the whole amount of the said above enumerated debts with interest thereon are paid in full"; that the trustee is to apply income "to the payment of interest and the liquidation of the principal amount of said indebtedness" and "of said notes"; that if and when payment in full is effected, the assets shall be distributed to the will beneficiaries and not to the certificate holders; that the "notes to be made by said trustee to evidence said indebtedness shall draw interest" at 6% payable semi-annually; that the certificate holders are designated as "creditors" or "claimants"; that the proceeds of the sale of any stock shall be applied first "for the payment or liquidation of said Trustee's notes and interest thereon, and distribute the balance to the beneficiaries under the will"; and that the "trust shall continue until such time as all of said Trustee's notes" and "accumulated interest" are paid in full; (b) The instrument's "declaration" portion's providing for the execution of "such notes and instruments to the several abovenamed creditors * * * with interest thereon" for the trustee's payments "in

liquidation of said debts", and for the application of income upon "current interest" and the surplus "above said interest" upon the principal "of said obligations"; (c) Each trust certificate's recital that it represents "a claim" and "is to draw interest" and that when the interest and principal of the claims have been paid in full the "certificate shall have no more value"; (d) The trustee's final state court report's recital that the claims "drew interest", that "the total amount of the debt set up in said trust" was still more than $27,000, that the trustee had distributed "the money in said trust, as it was received, to the several creditors", that the will beneficiaries received nothing, and that "Your trustee further states and shows that it has in fact been more or less nothing but an assignee of certain assets for the benefit of creditors; in fact, that was the only purpose of the contract * * *"; (e) The report's exhibits showing distributions "to the creditors" and the amounts of the "claims" from time to time, with additions of "interest", and payments made; (f) The waiver, filed with the state court, describing its signers as "creditors of the above trust"; (g) The state court's order closing the trusteeship reciting that it had for hearing the final report of the bank "described as a trustee, but in fact an assignee for the creditors in the estate of W. N. Merritt" and that "the creditors or beneficiaries of the bank trust, have all filed releases"; and (h) The court's finding that "the bank trust was in fact an assignment for the benefit of creditors rather than a trust".

The trust agreement did authorize the "surrender and release" of the six creditors' respective claims against the estate in payment for the Polk County real estate. This, however, we do not construe and interpret as effecting a novation or basic change in the posture of the six creditors and their successors. Their interests were still in the nature of claims definite in amount and with a specified

interest rate. Instead of being applicable to all the assets of the decedent's estate, these became confined to those fewer assets which had come from the estate to the trustee by way of the "purchase" and pursuant to the understanding reached by all concerned. The release of the claims therefore had significance only as it freed untransferred assets of the estate from the claims of the six major creditors. These creditors' claims were still directed to the transferred assets.

Neither do we regard as opposingly significant the quit claim deed executed by the will beneficiaries in 1952, before the taxpayer's acquisition of the two certificates in 1954 but after the coal mining operations had ceased. Its apparent purpose, it seems to us, was that of title clarification in anticipation of the real estate sale on which Mr. Breen, as president of Urbandale, was hard at work. Had the deed been intended to operate as a release of the will beneficiaries' interests under the agreement, it is reasonable to suppose that broader provisions to that effect would have been forthcoming.

In summary, the arrangement smacks throughout of indebtedness and of an assignment for the benefit of creditors. It appeared indisputably so at its inception and nothing that took place later convinces us that any change of character was effected. The taxpayer himself was the draftsman of most of the pertinent instruments. We doubt whether their language was unfortunately and unintendedly "loose", as the taxpayer would now describe it. We regard it as truthfully representative of the situation as it existed in 1930 and as it continued to exist thereafter. The taxpayer's services culminated in a happy and amazingly successful result for the certificate holders including himself. But that fact does not change the essential char-

acter of those services. See, generally, *Thomas* v. *Perkins*, 108 F.2d 87 (5 Cir. 1939).

Affirmed.

A true copy.

Attest:

Clerk, U. S. Court of Appeals, Eighth Circuit.

APPENDIX B

(Filed February 26, 1964. Robert C. Tucker.)

Judgment

United States Court of Appeals

FOR THE EIGHTH CIRCUIT

No. 17,308. September Term, 1963.

Maurice J. Breen and Alyce J. Breen, *Petitioners*,
vs.
Commissioners of Internal Revenue.

On Petition for Review of Decision of The Tax Court of the United States.

This cause came on to be heard on the Petition to review the Decision of The Tax Court of the United States entered on December 10th, 1962, determing that there are deficiencies in the income taxes of petitioners for the taxable years 1955 and 1956, and was argued by counsel.

On Consideration Whereof, It is now here Ordered and Adjudged by this Court that the Decision of The Tax Court of the United States in this cause be, and the same is hereby, affirmed.

And it is further Ordered by this Court that the Petition to review in this cause be, and the same is hereby, dismissed.

February 26, 1964.

Order entered in accordance with Opinion:

Robert C. Tucker
Clerk, U. S. Court of Appeals
for the Eighth Circuit.

APPENDIX C

This is the portion of the Tax Court Opinion that is relevant. The Taxpayer appealed to the Tax Court on four separate matters, and was successful, or relatively so, on two, which were not too important. The taxpayer appealed the two questions that he lost, to the Circuit Court of Appeals, and the Commissioner appealed from the ruling on the two that were unfavorable to him, and he afterwards dismissed his appeal.

The pages in the part of the Opinion used are identical with the original Opinion of the Tax Court.

T. C. Memo. 1962-230

TAX COURT OF THE UNITED STATES
MAURICE J. BREEN and ALYCE BREEN,
Petitioners,

v.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

Docket No. 85016. Filed September 28, 1962.

Opinion

The first issue is whether section 1301[2] applies to the

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2. SEC. 1301. COMPENSATION FROM AN EMPLOYMENT.

(a) Limitation on Tax.—If an individual or partnership—

(1) engages in an employment as defined in subsection (b); and

(2) the employment covers a period of 36 months or more (from the beginning to the completion of such employment); and

(3) the gross compensation from the employment received or accrued in the taxable year of the individual or partnership is not less than 80 percent of the total compensation from such employment,

titioner's services for the coal corporation were either (1) part of his overall efforts as executor and trustee to conserve the assets of the Merritt estate, or (2) a separate undertaking to perform general services in the employment of an operating corporation. If the first interpretation is true, the respondent argues that the $4,200 payment in 1955 fails to meet the 80 percent test of section 1301 because petitioner had been paid trustee and executor fees from 1928 through 1945 of about $12,600, plus an interest in certain property. If the second interpretation is true, then respondent contends that the services of petitioner for the coal corporation do not come within the definition of "an employment" within the meaning of section 1301.

Petitioner contends that the $4,200 was not paid to him as a part of his overall compensation for services performed for the Merritt estate or for the benefit of beneficiaries or creditors of that estate or for trustees holding assets of

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then the tax attributable to any part of the compensation which is included in the gross income of any individual shall not be greater than the aggregate of the taxes attributable to such part had it been included in the gross income of such individual ratably over that part of the period which precedes the date of such receipt or accrual.

(b) Definitation of an Employment.—For purposes of this section, the term "an employment" means an arrangement or series of arrangements for the performance of personal services by an individual or partnership to effect a particular result, regardless of the number of sources from which compensation therefor is obtained.

$4,200 received by petitioner in 1955 from the Urbandale Coal & Acreage Company.[3] Respondent argues that pe-

3. Although petitioner specifically claimed the benefit of section 1301 in his 1955 income tax return, the respondent in his notice of deficiency, did not mention section 1301 but stated that *section 1303* was not applicable. However, in the petition and answer the parties indicate that the issue as to this item is the applicability of section 1301.

that estate. He contends the payment was made by the corporation for services he performed for the corporation as president and director during 21 years of its corporate existence.

Without reviewing the evidence, we will accept petitioner's contention and this means the statute is applicable if, in performing such services as president and director of the corporation, he was engaged in "an employment" as that term is defined in the statute. Section 1301 (b), as here applicable, defines the term as meaning "an arrangement * * * for the performance of personal services * * * to effect a particular result * * *." In his regulations the Commissioner has, we think, correctly pointed out that "an arrangement to perform general services is not an employment within the meaning of section 1301 either as to any particular project on which services are performed or as to the general services since there is no understanding that the services are to accomplish a particular result." Section 1.1301-2(b), Income Tax Regs. The question of whether "an employment" within the meaning of the statute exists is one of fact and the Commissioner's regulation states that "(t)he primary factor in making such a determination is what the particular profession, business, or industry would normally consider as a distinct project or result." Section 1.1301-2(b) (ii), Income Tax Regs.

Would engagement to serve as president and director of an operating corporation be normally considered by business or industry as engagement in a distinct project to effect a particular result as distinguished from general employment to render general services for the corporation? We think not. When we consider the particular facts and circumstances surrounding the employment contract in this case or the understanding of the parties to see if there was engagement to effect a particular result (Sec. 1.1301-2

(b) (ii)), we reach the same conclusion. We find nothing in the record to indicate petitioner was engaged to render, or that he performed, services for the corporation beyond the normal duties of president and director of an operating company. The corporate minutes that authorized the payment to the two officers recite the payment is "for their services as directors, and their services in attending board meetings and committee meetings, and other incidental work connected with the management of said corporation." The $4,200 was paid to petitioner for services that were performed in prior years but this statute is not applicable when the employment was general and not designed to effect a particular result.[4] We hold for respondent on the issue. The $4,200 was fully taxable in the year of receipt.

The next issue is whether the gains realized by petitioner in 1955 and 1956 from the retirement of the two trustee's certificates held by him are taxable as capital gains or ordinary income. The trustee arrangement executed in 1930 was in the nature of an assignment for the benefit of the major creditors of the Merritt estate. The trustee-bank held the stock in the Urbandale Coal & Acreage Company as security for the claims of the creditors who each received a trust certificate representing a proportional interest in the trust.

Petitioner purchased two of these trustee's certificates in April 1954, one representing a .4666 interest for the sum of $2,500, the other representing a .0384 interest for $150.

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4. Ordinarily salary or compensation for personal services is taxable in the year of receipt even though services were performed in prior years. Section 1303 gives some tax relief for back pay received in a taxable year when payment of compensation is delayed by bankruptcy of employer or some similar event. Here petitioner testified the corporation was solvent and he does not argue section 1303 is applicable.

He received payments of $8,258 in 1955 and $13,334.41 in 1956 from the trustee-bank to be applied to the two certificates. These payments were made in the liquidation of the trust.

These trustee certificates were nothing more than evidences of indebtedness. In the trust agreement executed in 1930 these instruments are referred to throughout as "notes". In fact, the trustee certificates themselves do not purport to do anything more than represent outstanding claims, as the following excerpt from one of the certificates purchased by petitioner shows:

> This certificate represents a claim of $12,923.92, which sum is to draw interest at the rate of 6 per annum to be computed March 1st and September 1st of each year and all of that portion of the sums paid by the trustee on said dates in excess of the interest then due shall be endorsed upon the principal of said claim and when said interest and principal have been paid in full through the disbursements of said trustee, then this certificate shall have no more value.

To obtain capital gains treatment for a realized gain there must be, in addition to other requirements, a "sale or exchange". Section 1222. The payments which petitioner received in 1955 and 1956 were not payments received in any sale transaction of his trust certificates. They were payments made by the trustee-bank in accordance with the terms of the trust obligation. It can be conceded that the trust certificates were capital assets in the hands of petitioner and that he held them more than 6 months. But the sums he received from the trustee-bank were not received as the result of any sale or exchange of the certificates. See *Ogilvie* v. *Commissioner*, 216 F.2d 748, affirming 20 T.C. 734; *Pat N. Fahey*, 16 T.C. 105; *Lee* v. *Commissioner*, 119 F.2d 946, affirming 42 B.T.A. 920, and *Samuel Towers*, 24 T.C. 199, affirmed 247 F.2d 233.

Moreover, it appears that the total payments on the trustee's certificates since 1931 went for the most part to meet the interest on the outstanding claims. Originally, the claims represented by the certificates totaled $25,570.70 and that although the total payments to the certificate holders from 1931 through January 16, 1956 (the date of final payment) totaled $58,296.03, the total debt still outstanding as of January 16, 1956, was $27,018.71. It would seem then that the payments to the certificate holders, including petitioner, largely represent interest payments.

We hold for the respondent on this issue.

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In the Supreme Court of the United States

OCTOBER TERM, 1964

No. 155

MAURICE J. BREEN and ALYCE J. BREEN, PETITIONERS

v.

COMMISSIONER OF INTERNAL REVENUE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE EIGHTH CIRCUIT

BRIEF FOR THE RESPONDENT IN OPPOSITION

OPINIONS BELOW

The memorandum opinion of the Tax Court (Pet. A18-A23) is not officially reported. The opinion of the Court of Appeals (Pet. A1-A16) is reported at 328 F. 2d 58.

JURISDICTION

The judgment of the Court of Appeals (Pet. A17) was entered on February 26, 1964. The petition for a

writ of certiorari was filed on June 5, 1964, after entry of an order of April 30, 1964, by Mr. Justice White, extending until June 25, 1964, the time for filing the petition. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

QUESTIONS PRESENTED

1. Whether the personal services for which the taxpayer received a payment of $4,200 during the taxable year 1955 constitute an "employment" within the definition of Section 1301 of the 1954 Code, so as to entitle the taxpayer to the income-spreading benefits there provided.

2. Whether gains received by the taxpayer during 1955 and 1956 with respect to two "trustee's certificates" which he purchased in 1954 represented payments made to him as a creditor-claimant against the trust property and therefore taxable as ordinary income, or whether they represented payments in liquidation of an equity ownership in such property and therefore taxable as long term capital gains.

STATUTE AND REGULATIONS INVOLVED

The relevant portions of the Internal Revenue Code of 1954, Sections 302, 317, 331, 652, 662 and 1301, and the Treasury Regulations on Income Tax (1954 Code) Section 1.1301-2, are set forth in the Appendix, *infra*.

STATEMENT

W. N. Merritt died in May, 1928. Among his assets at his death were undivided interests in two tracts of real estate near Des Moines, in Polk County, Iowa. These were heavily mortgaged. The taxpayer, a practicing lawyer, was named as executor and trustee in the decedent's will. (Pet. A2.)

The assets of Merritt's estate were insufficient to meet the claims of creditors. In September, 1930, a "Trust Agreement and Appointment of Attorney in Fact" was executed by the six major creditors, whose claims aggregated about $27,500, the will beneficiaries, and a bank as trustee. This agreement provided that (a) the six creditors released their claims against the estate; (b) the trustee assumed the title to the decedent's interests in the Polk County real estate and to certain stock not significant here; (c) the release of the claims was the purchase price for that property; (d) the trustee was authorized to convey the real estate interests so received to Urbandale Coal and Acreage Company,[1] a newly organized Iowa corporation, in exchange for half its stock; (e) the trustee was to hold that stock as trust property "and as security for notes evidencing the * * * indebtedness" to the creditors and to apply income of the trust in payment of interest and principal; (f) Urbandale was to receive, in exchange for the other half of its stock, equal undivided interests owned by attorney D. M. Kelleher in the same real estate; and (g) the

[1] Hereinafter referred to as Urbandale.

trustee was to hold the trust property until the indebtedness to creditors and the interest thereon were "paid in full, and thereafter hold the same for distribution to * * * the beneficiaries under the will of said W. N. Merritt in the proportions they are entitled to share in the Estate of said Testator". (Pet. A2-A3.)

The trustee issued a certificate to each of the six creditors. This recited that the creditor was the owner of a stated percentage "of the equitable ownership and beneficial interest in" the stock, including preferred and common of Urbandale, held by the trustee "for the benefit of the holder or holders of this certificate and all similar certificates issued"; that "when said interest and principal have been paid in full through the disbursements of said trustee, then this certificate shall have no more value"; and that the certificate "may be assigned and transferred". (Pet. A3.)

Almost 24 years later, in April, 1954, the taxpayer purchased for $2,500 one of the trustee's certificates representing a 46.66 per cent interest in the trust and an original creditor's claim of $12,932.92. A week later the taxpayer purchased for $150 a second certificate representing a 3.84 per cent interest and a creditor's claim of $1,050. (Pet. A3.)

Meanwhile, through a working mining company, Urbandale operated the coal mine on the Polk County land on a royalty basis until 1947. In December, 1952, the Merrit estate beneficiaries gave Urbandale a quitclaim deed to the land. (Pet. A3.)

During this entire period the taxpayer was president of Urbandale, Kelleher was vice-president, and

Mrs. Kelleher was secretary-treasurer. These three also comprised the directorship of the corporation during its corporate life. (Pet. A4.)

When the mining operations ceased, the taxpayer, as president of Urbandale, began to negotiate for the sale of the land, and sold it late in 1954. Urbandale then adopted a resolution to liquidate. In March, 1955, Urbandale's shareholders approved payment of a $4,200 fee to the taxpayer and of a like fee to Mrs. Kelleher. The authorizing resolution stated that, throughout its corporate existence of more than 24 years, no compensation had ever been paid to any officer or director (Pet. A4) and

> (1) That the said Maurice J. Breen and Mary S. Kelleher, each, be allowed the sum of $200.00 a year for their services as directors, and their services in attending board meetings and committee meetings, and other incidental work connected with the management of said corporation.
>
> (a) That said allowance extend over the first twenty-one years of the life of this corporation, as said twenty-one years covers the active operation of this corporation while it was engaged in the production of coal, and that said allowance to each of said named directors, to wit, Mary S. Kelleher and Maurice J. Breen, be in the sum of $4200.00 each.

The taxpayer's $4,200 fee was paid in 1955. Except for a $500 fee paid in December, 1949 for legal services on a special matter, the taxpayer had received no other compensation from Urbandale (Pet. A4.)

The trustee, from 1931 through 1956, made payments to the certificate holders. These were distributions from the coal royalties and upon the liquidation. The taxpayer received approximately $8,250 in 1955, and $13,350 in 1956, upon the two certificates he had purchased in 1954, and thereby realized gain. (Pet. A5.)

The taxpayer, on his return for 1955, reported the $4,200 fee under the income-spreading provisions of Section 1301 of the Internal Revenue Code of 1954, *infra*, and, on the 1955 and 1956 returns, reported as capital gain his gain on the respective distributions of $8,250 and $13,350. The Commissioner asserted deficiencies on several bases, including the disallowance of the spreading of the $4,200 and the capital gain treatment. Upon petition for redetermination, the Tax Court decided for the taxpayer upon several of the issues presented but sustained the Commissioner's ruling with respect to income spreading and capital gain treatment (Pet. A18-A23). The Eighth Circuit affirmed the Tax Court's disposition of these two issues.

ARGUMENT

1. The Court of Appeals correctly held that the $4,200 paid taxpayer in 1955 by Urbandale was intended as compensation for general managerial services rendered the corporation (Pet. A8-A9), and that such services did not constitute an "employment" within the meaning of Section 1301(b) of the Internal Revenue Code of 1954. Accordingly, the court properly denied him the income-spreading benefit provided in that section.

The taxpayer's initial argument (Pet. 18) is that the predecessor of Section 1301 (Section 107 of the 1939 Code) had been applied in other cases so as to authorize income spreading in connection with compensation for general managerial services to a corporation and that the new and more specific qualifying provisions of Section 1301 do not import a narrowing of coverage. But the fact is that, whereas Section 107(a) of the 1939 Code required only that the compensation be for "personal services", Section 1301(b) of the 1954 Code is much more limited and requires that it be received for "personal services * * * to effect a particular result". Accordingly, the Court of Appeals ruled (Pet. A11) that, whatever the 1939 Code provision may have meant, the clear language of the current provision does not embrace general corporate managerial services but requires that the income be received for services looking forward to the production of a particular, specific result. This construction is entirely consonant with the language of the statute, with the ruling of the Sixth Circuit in *Ranz* v. *Commissioner*, 273 F. 2d 810, and with applicable Treasury Regulations,[2] and there is no conflict of authority.[3]

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[2] Treasury Regulations on Income Tax (1954 Code), Section 1.1301-2(b)(1)(i), *infra*, provide that "an arrangement to perform general services is not an employment within the meaning of section 1301 either as to any particular project on which services are performed or as to the general services since there is no understanding that the services are to accomplish a particular result."

[3] *Wattley* v. *Commissioner*, 275 F. 2d 461 (C.A. 2d), cited by taxpayer (Pet. 18), does not constitute a contrary holding

The taxpayer also argues (Pet. 23-24) that, even if the 1954 Code bars his claim, it is covered by the more general terms of the 1939 Code because the services in question were, for the most part, performed during years prior to the effective date of the 1954 language, which (see Section 7851(a)(1)(A) of the 1954 Code) governs tax years beginning after December 31, 1953. But the appellate court correctly held (Pet. A7) that the case was ruled by the law in effect in 1955 (Pet. A4) when the income in question was received and not the law of earlier years during which it was earned. The taxpayer's reliance (Pet. 23-24) upon general statements that legislation altering substantive rights is not to be applied retroactively is misplaced since there was here no retroactive application. At issue was the taxpayer's liability for the year 1955—not the earlier years. Cf. *McClure* v. *United States*, 228 F. 2d 322, 324 (C.A. 4th); *Ranz* v. *Commissioner*, *supra* (where, also, most of the services were performed prior to the effective date of the 1954 Code).

Finally, the taxpayer contends (Pet. 18, 21-23) that his services to Urbandale were not of a general

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since (1) the court there had before it only tax years coming under the 1939 Code language, (2) the court's comment (p. 464) that Congress did not, in enacting Section 1301, appear to have intended to change the meaning of Section 107(a) was addressed to a question not here involved (whether a period of efforts as a representative of a corporation can be joined together with subsequent efforts as an individual in fixing the period of "personal services"), and (3) even this comment was merely a *dictum*, the court expressly refraining (p. 465) from deciding that question.

nature but were intended to accomplish a specific result—the liquidation of the company through the sale of the land. This is no more than a factual contention which the courts below rejected (Pet. A8-A9, A20-A21) on the basis of the record. The recitation by the Court of Appeals (Pet. A8-A9) reflects more than ample evidence to sustain the crucial finding and a factual question of this nature, significant only with respect to the case at bar, is not such as to warrant review by this Court.

2. With respect to the issue involving the tax treatment to be accorded the gains received by him during 1955 and 1956 arising out of the two "trustee's certificates" which he purchased in 1954, the taxpayer in effect asks this Court to determine whether certain instruments embodying conflicting terminology should more reasonably be construed as investing him with an ownership rather than with a creditor status.

Although the taxpayer invokes (Pet. 25, 26, 28, 36) certain sections of the Internal Revenue Code of 1954 (Sections 302, 331, 652 and 662, Appendix, *infra*), there is actually no disagreement as to the purport of those provisions. The cumulative effect of the above-cited sections of the Code, so far as here relevant, is (1) that a redemption of corporate stock shall be deemed an exchange between the redeeming corporation and the shareholders who surrender their stock to it and (2) that where amounts distributed to a beneficiary of a trust constituted capital gains

in the hands of the trustee, they shall be similarly treated in the hands of the beneficiaries.[4] But these provisions, by their terms, apply only where the income recipients were the legal or beneficial *owners* of the stock which was redeemed. Neither the Commissioner nor the courts below questioned that the amounts involved would qualify for capital gains treatment were this condition met, and the taxpayer has never denied the existence or the validity of the condition. Thus, the meaning of these sections of the Code has never been contested. The courts below denied the taxpayer's claim to capital gain treatment solely upon the holding (Pet. A13-A15, A21-A22) that he stood, really, in the position of creditor-claimant against the trust property, rather than that of a beneficial owner thereof. This controlling determination represented no more than a choice between conflicting contentions as to the intended relationship between the trust and the six creditors of the estate, as manifested by the language and actual provision of the several instruments. No question of law was involved and there was ample support (see Pet. A13-A15, A21-A22) for the courts' factual determination.

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[4] It should be noted that the latter provision is found in Sections 652 and 662 of the Code; the taxpayer did not, in the court below, cite these sections or rely upon this provision. It is doubtful, therefore, whether he may now ask this Court to consider them for the first time. See *Knetsch* v. *Commissioner*, 364 U.S. 361, 370. Section 652 is not, in any event, relevant since it does not deal with a distribution of corpus.

CONCLUSION

For the above reasons, the petition for a writ of certiorari should be denied.

Respectfully submitted.

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JULY, 1964.

APPENDIX

Internal Revenue Code of 1954 (26 U.S.C.):

SEC. 302. DISTRIBUTIONS IN REDEMPTION OF STOCK.

(a) *General Rule.*—If a corporation redeems its stock (within the meaning of section 317(b)), and if paragraph (1), (2), (3), or (4) of subsection (b) applies, such redemption shall be treated as a distribution in part or full payment in exchange for the stock.

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SEC. 317. OTHER DEFINITIONS.

* * * *

(b) *Redemption of Stock.*—For purposes of this part, stock shall be treated as redeemed by a corporation if the corporation acquires its stock from a shareholder in exchange for property, whether or not the stock so acquired is cancelled, retired or held as treasury stock.

SEC. 331. GAIN OR LOSS TO SHAREHOLDERS IN CORPORATE LIQUIDATIONS.

(a) *General Rule.*—

(1) *Complete liquidations.*—Amounts distributed in complete liquidation of a corporation shall be treated as in full payment in exchange for the stock.

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SEC. 652. INCLUSION OF AMOUNTS IN GROSS INCOME OF BENEFICIARIES OF TRUSTS DISTRIBUTING CURRENT INCOME ONLY.

(a) *Inclusion.*—Subject to subsection (b), the amount of income for the taxable year required to be distributed currently by a trust described in section 651 shall be included in the gross income of the beneficiaries to whom the income is required to be distributed, whether distributed or not. * * *

(b) *Character of Amounts.*—The amounts specified in subsection (a) shall have the same character in the hands of the beneficiary as in the hands of the trust. * * *

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SEC. 662. INCLUSION OF AMOUNTS IN GROSS INCOME OF BENEFICIARIES OF ESTATES AND TRUSTS ACCUMULATING INCOME OR DISTRIBUTING CORPUS.

(a) *Inclusion.*—Subject to subsection (b), there shall be included in the gross income of a beneficiary to whom an amount specified in section 661 (a) is paid, credited, or required to be distributed (by an estate or trust described in section 661), the sum of the following amounts:

* * * *

(b) *Character of Amounts.*—The amounts determined under subsection (a) shall have the same character in the hands of the beneficiary as in the hands of the estate or trust. * * *

* * * *

SEC. 1301. COMPENSATION FROM AN EMPLOYMENT.

(a) *Limitation on Tax.*—If an individual or partnership—

(1) engages in an employment as defined in subsection (b); and

(2) the employment covers a period of 36 months or more (from the beginning to the completion of such employment); and

(3) the gross compensation from the employment received or accrued in the taxable year of the individual or partnership is not less than 80 percent of the total compensation from such employment,

then the tax attributable to any part of the compensation which is included in the gross income of any individual shall not be greater than the aggregate of the taxes attributable to such part had it been included in the gross income of such individual ratably over that part of the period which precedes the date of such receipt or accrual.

(b) *Definition of an Employment.*—For purposes of this section, the term "an employment" means an arrangement or series of arrangements for the performance of personal services by an individual or partnership to effect a particular result, regardless of the number of sources from which compensation therefor is obtained.

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Treasury Regulations on Income Tax (1954 Code) (26 C.F.R.):

Sec. 1.1301-2. *Compensation from an employment.*

* * * *

(b) *Definition of an employment.* (1)(i) The term "an employment" means an arrangement or series of arrangements for the performance of personal services by an individual or partnership to effect a particular result, regardless of the number of sources from which compensation for such services is obtained. Thus, there must be an arrangement, and the arrangement must be for the performance of a particular project. In other words, there must be an understanding for the performance of services to accomplish a particular result. Accordingly, an arrangement to perform general services is not an employment within the meaning of section 1301 either as to any particular project on which services are performed or as to the general services since there is no understanding that the services are to accomplish a particular result.

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